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In the Supreme Court of the United States

OCTOBER TERM, 1936

No. 330

THE UNITED STATES, PETITIONER
v.
AUTOMATIC WASHER COMPANY

ON WRIT OF CERTIORARI TO THE COURT OF CLAIMS

BRIEF FOR THE UNITED STATES

OPINION BELOW

The opinion of the Court of Claims (R. 10–13) is reported in 15 F. Supp. 70.

JURISDICTION

The judgment of the Court of Claims was entered June 1, 1936 (R. 13). The petition for a writ of certiorari was filed September 1, 1936, and was granted October 19, 1936. The jurisdiction of this Court rests on Section 3 (b) of the Act of February 13, 1925.

QUESTION PRESENTED

The assets of A corporation were conveyed to respondent corporation which agreed to deliver its

stock therefor directly to A's stockholders. Pursuant to the stockholders' direction, respondent issued certificates for part of the stock in the name of an individual appointed by the stockholders as their attorney in fact in the sale thereof for their account. Did this transaction involve a taxable transfer by the stockholders within the meaning of Section 800, Schedule A–3 of the Revenue Act of 1926?

STATUTES AND REGULATIONS INVOLVED

These are set forth in the Appendix, *infra,* pp. 20–22.

STATEMENT

This action was brought by respondent to recover documentary stamp taxes. The case was submitted upon an agreed stipulation of facts, and the findings of the Court of Claims may be summarized as follows:

Respondent, a Delaware corporation, hereinafter sometimes referred to as the "new company", was organized in June, 1928, to engage in the manufacture of electric washing machines. It succeeded to the business and assets of the Automatic Washer Company, an Iowa corporation, hereinafter referred to as the "old company." (R. 5.)

On June 22, 1928, an agreement was entered into between one Nelson, a stockholder and officer of the old company, and Folds, Buck and Company, Bankers, whereby Nelson proposed to reorganize the old company by organizing a new corporation

under the laws of Delaware to acquire all the assets of the old company. The agreement provided that the authorized capital of the new company was to consist of 180,000 shares of common stock and 10,000 shares of convertible preference stock, both without par value, and the Bankers were given the option and privilege of purchasing the 40,000 shares of convertible preference stock and 40,000 shares of the common stock for $1,000,000. (R. 5–6.)

Pursuant to this agreement, the respondent corporation was thereafter organized (R. 6).

On September 17, 1928, all stockholders of the old company executed instruments appointing Nelson and one Gallagher their attorneys in fact to vote the stock of the old company at a special stockholders' meeting to be held on September 27, 1928, and to receive all dividends declared by the old company by way of liquidation or otherwise; to sell or dispose of for the stockholders all assets so received, including all or any part of the shares of stock of the new company accruing to them or to which they were or might become entitled by reason of any such reorganization. The attorneys in fact were directed by the instruments to sell and dispose of any or all such shares of stock in consummating the previous agreement between Nelson and the Bankers. Each instrument recited that in consideration of Nelson having made an agreement or agreements with the Bankers for the benefit of all stockholders of the old company in reliance upon their promise to execute and deliver "this proxy and power of

attorney", it should continue in effect until November 15, 1928, and be irrevocable. (R. 8.)

On September 27, 1928, respondent entered into an agreement with the old company whereby it was provided that all assets of the old company should be conveyed to respondent, which would assume all the liabilities of the old company, in consideration for the delivery by respondent of 140,000 shares of its common and 34,538 shares of its convertible preference stock to the stockholders of the old company, who (the agreement recited) had agreed among themselves that they would contribute all their convertible preference stock and 40,000 shares of their common stock for sale and delivery to the Bankers under the agreement of June 22, 1928, between Nelson (acting as agent for all of the stockholders) and the Bankers; that in order to carry out the plan, "whereby the stockholders of the Old Company will sell and deliver to the said Bankers" the 74,538 shares, each stockholder had appointed Nelson and Gallagher his attorneys in fact to receive the "securities" in respondent to which such stockholder might be entitled, and to receive the purchase price for such shares and distribute to the stockholders the proceeds of sale, after deducting all expenses. (R. 6–7.) The agreement further recited that respondent (R. 7)—

> in making delivery to the stockholders of the Old Company of the shares of stock agreed to be delivered as consideration for the ac-

> quisition of the property and assets of the Old Company shall issue such certificates in such names and for such amounts as shall be specified in the joint order of the said H. E. Nelson and W. N. Gallagher, the attorneys in fact for each of the stockholders of the Old Company, and deliver the same to said attorneys in fact, and certificates evidencing 34,538 shares of convertible preference stock and 40,000 shares of common stock shall be delivered by said attorneys in fact to or upon the order of Folds, Buck & Co., upon receipt of the sum of $868,912.00 * * *.

The agreement then recited that thereupon the $868,912 should be distributed proportionately among the stockholders, after deduction of expenses. (R. 6–8.)

On October 1, 1928, the old company transferred to respondent all assets and properties subject to all liabilities, and respondent thereupon issued certificates for 100,000 shares of its common stock to the individual stockholders of the old company in proportion to their holdings in the old company; certificates for 40,000 shares of common stock to Nelson, pursuant to the aforesaid powers of attorney (of which 7,069 shares were Nelson's pro rata portion as a stockholder of the old company); and certificates for 34,538 shares of its convertible preference stock to Nelson, pursuant to the aforesaid powers of attorney (of which 6,104 shares were Nelson's pro rata portion as a stockholder of the

old company). Nelson thereupon transferred to the Bankers the 40,000 shares of common and 34,538 shares of preference stock, collected the proceeds therefor, and made distribution thereof among the stockholders of the old company. (R. 8–9.) The remaining 40,000 shares of authorized common stock were to remain in respondent's treasury (R. 6). Gallagher did not act with Nelson in the transaction. Nelson acted alone. (R. 11.)

Respondent duly paid the stamp tax on the original issue of 140,000 shares of common and 34,538 shares of preference stock. It also paid the stamp tax on the subsequent transfer by Nelson to the Bankers of the 40,000 shares of common and 34,538 shares of preference stock. (R. 9.)

Thereafter, two additional stamp taxes were demanded and collected from respondent, one of $4,020.46 on the transfer by the old company to its stockholders of its right to receive from respondent 140,000 shares of common and 34,538 shares of preference stock, and one of $1,593.63, including interest and penalty, on the transfer by the stockholders of the old company to Nelson of their rights to receive the 40,000 shares of common and 34,538 shares of preference stock for which certificates were issued by respondent in the name of Nelson for transfer and sale to the Bankers. (R. 9.)

The validity of the $4,020.46 tax on the transfer by the old company to its stockholders of its right to receive the 174,538 shares of respondent's stock was conceded in the court below and claim there-

for abandoned by respondent, on the authority of *Raybestos-Manhattan Co.* v. *United States,* 296 U. S. 60. (R. 9, 12.)

On June 12, 1931, respondent filed a claim for the refund of $1,593.63, representing the tax on the transfer by the stockholders to Nelson with respect to the 40,000 shares of common and 34,538 shares of preference stock. The claim was rejected by the Commissioner on November 10, 1931 (R. 9–10).

Suit was brought in the Court of Claims on October 14, 1933 (R. 1), and on June 1, 1936, judgment was entered for respondent in the amount of $1,593.63, with interest (R. 13).

SPECIFICATION OF ERRORS TO BE URGED

The court below erred:

1. In holding that the transfer by the stockholders of the old company to their nominee of their right to receive stock in the new company was not subject to the stamp tax imposed by the Revenue Act of 1926.

2. In failing to hold that the transfer to Nelson of the stock ultimately sold to the Bankers was a taxable transfer under the statute.

3. In holding that respondent was entitled to recover $1,593.63, with interest, and entering judgment for respondent in said amount.

SUMMARY OF ARGUMENT

There was a taxable transfer by the stockholders of the old company to their attorney-in-fact of legal

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title to, or rights to receive, shares of stock and certificates therefor in the new corporation.

Under the corporate agreement of September 27, 1928, there accrued to the old company the right to receive all the shares of stock to be issued by respondent as consideration for its assets. By the same instrument, that right to receive the shares, and to become stockholders, was transferred to the stockholders of the old company. Immediately upon conveyance of the assets of the old company to respondent, the stockholders of the old company were vested with legal title to, and/or the right to receive, such stock and certificates evidencing the stock. This is recognized in the agreement itself and in the concession of respondent in the court below that there was a transfer by the old corporation to its stockholders of the right to receive shares of stock within the decision in *Raybestos Manhattan Company* v. *United States,* 296 U. S. 60.

The stock and rights so vested in the stockholders were transferred by them to their attorney-in-fact. As part of the plan of reorganization, the stockholders had agreed to sell and deliver a portion of the new shares to a firm of bankers. To carry out this purpose the stockholders directed the issuance of part of the stock in the name of an individual designated by them, who was directed by them to execute the sale and make distribution of the proceeds to the stockholders. By directing the issuance of the stock and certificates in the name of their attorney-in-fact, the

stockholders transferred to him legal title to, and/or their rights to receive, the stock and certificates therefor. Should the nomination of such attorney-in-fact, without more, be deemed insufficient to effect a taxable transfer, the subsequent issuance of the certificates to such attorney effectively completed the transfer of the stockholders' rights and title.

ARGUMENT

Section 800, Schedule A–2 of the Revenue Act of 1926, imposes a stamp tax on the original issue of shares of corporate stock. By Section 800, Schedule A–3, a like tax is laid—

> On all sales, or agreements to sell, or memoranda of sales or deliveries of, or transfers of legal title to shares or certificates of stock or of profits or of interest in property or accumulations in any corporation, or to rights to subscribe for or to receive such shares or certificates, whether made upon or shown by the books of the corporation, or by any assignment in blank, or by any delivery, or by any paper or agreement or memorandum or other evidence of transfer or sale, *whether entitling the holder in any manner to the benefit of such stock, interest, or rights, or not,* * * *. [Italics supplied.]

Section 800 imposes liability for the tax upon the transferor, the transferee and the corporation whose stock is transferred. *Raybestos-Manhattan Co.* v. *United States,* 296 U. S. 60, 61.

Respondent corporation was organized in 1928, to take over the assets and business of its predecessor, the Automatic Electric Washer Company, in consideration for the delivery of 174,538 shares of its capital stock to the stockholders of the old company. As the result of a special meeting of all stockholders, represented by their proxy to Nelson, the old company on September 27, 1928, entered into a written agreement with respondent, pursuant to which on October 1, 1928, all assets of the old company were conveyed to respondent, which assumed all liabilities of the old company.

In addition to the original issue tax paid under Schedule A–2, two transfer taxes were collected under Schedule A–3, one on the transfer by the old company to its stockholders of its right to receive the shares, and one on the transfer from the stockholders to Nelson of their rights to receive part of the shares. The correctness of the first of these two taxes has been conceded by respondent (R. 9, 12). Only the last-mentioned tax is here in issue.

We contend that the Commissioner's determination was correct as to 61,365 of the 74,538 shares for which certificates were issued to Nelson, for the reason that there was transferred from the stockholders to Nelson their legal title to and/or their rights to receive such shares, and certificates therefor. We make no contention with respect to the 13,173 shares representing Nelson's own proportionate interest as a stockholder of the old company. (R. 13.)

Respondent apparently contends (Br. in Opp. pp. 2–3) that the stockholders never acquired a right to receive the 61,365 shares for which certificates were issued to Nelson; that, in fact, such rights had been relinquished by the powers of attorney executed by the stockholders on September 17, 1928; and that therefore the stockholders did not transfer and could not have transferred any rights within the purview of Schedule A–3. We submit that this argument is answered by the terms of the powers of attorney and the corporate agreement, by the concession of the respondent properly made in the court below, and by the scope of the stamp tax provisions as set forth in *Raybestos-Manhattan Company* v. *United States,* 296 U. S. 60.

1. Every arrangement in the reorganization as planned and executed shows a meticulous regard for the fact that the stockholders had a right to receive the stock and transferred that right to their nominees.

The documents executed by the stockholders on September 17, 1928 (R. 8) appointed Nelson and Gallagher attorneys in fact for the stockholders, and conferred on them certain powers and duties. After conferring power of attorney to vote at the stockholders' meeting on September 27, 1928, the stockholders by these powers of attorney authorized and directed Nelson and Gallagher, in consummating the agreement between Nelson and the bankers, to sell certain shares of stock accruing to the stockholders or to which they were or might become en-

titled (R. 8). These powers of attorney, so far from constituting a relinquishment by the stockholders of the right to receive shares of stock, affirmed that right and undertook to confer upon the individuals selected by the stockholders themselves powers whose very existence depended upon a transfer of rights to them by the stockholders.

That the stockholders acquired the right to receive the shares in question and transferred their rights to their nominees is also the clear import of the subsequent agreement of September 27, 1928 between the old and new corporations.

The agreement executed September 27, 1928, expressly provided (R. 6–7):

> As consideration for such conveyance of said property and assets, the New Company *shall deliver to the stockholders of the Old Company* the following securities of the New Company:
>
> | | |
> |---|---|
> | Convertible Preference Stock (without any nominal or par value) | 34,538 shares |
> | Common Stock without nominal or par value | 140,000 " |
>
> Immediately upon the conveyance of all of the assets of the Old Company to the New Company, the stockholders of the Old Company shall be in control of the New Company * * * [Italics supplied.]

The agreement recited that, "as a part of the plan of reorganization, the stockholders of the Old Company have agreed among themselves that each will contribute" certain shares received by him in the new company, and that the shares so contrib-

uted (74,538) shall be sold and delivered to the Bankers, under the provisions of an agreement dated June 22, 1928, between Nelson, acting as agent for all of the stockholders, and the Bankers. The agreement also provided (R. 7):

> In order to carry out this plan whereby the *stockholders of the Old Company will sell and deliver to the said Bankers* said 34,538 shares of the convertible preference stock and 40,000 shares of the common stock of the New Company, *each of the stockholders of the Old Company has irrevocably constituted and appointed H. E. Nelson and W. N. Gallagher his attorneys in fact to receive the respective securities of the New Company to which such stockholder may be entitled and to make sale of that portion thereof to be contributed by such stockholder* for the purpose of carrying out said agreement of sale with the Bankers and to receive the purchase price for all of said shares of stock so sold and delivered to the Bankers, and distribute to each of the stockholders of the Old Company his proportionate share of the proceeds of such sale, after deducting all expenses of the said attorneys in fact therefrom.
>
> ***Accordingly, the New Company, in making delivery to the stockholders of the Old Company of the shares of stock agreed to be delivered as consideration for the acquisition of the property and assets of the Old Company*** shall issue such certificates in such names and for such amounts as shall be

> specified in the joint order of the said H. E. Nelson and W. N. Gallagher, the attorneys in fact for each of the stockholders of the Old Company, and deliver the same to said attorneys in fact, and certificates evidencing 34,538 shares of convertible preference stock and 40,000 shares of common stock shall be delivered by said attorneys in fact to or upon the order of Folds, Buck & Co., upon receipt of the sum of $868,912.00 (less the expenses to be deducted therefrom). [Italics supplied.]

Thus, by the agreement of September 27, 1928, the old company undertook to dispose and divest itself of all its corporate interests, rights, and accumulations, through a corporate distribution to its stockholders of the entire consideration payable for its assets, by causing respondent to pay and deliver such consideration directly to the stockholders in performance of respondent's obligation to the old company. *Rockefeller* v. *United States,* 257 U. S. 176. Under the agreement, the consideration was not intended to be distributed to the stockholders part in stock and part in cash, but was to be in the form of delivery to them by respondent of all the 174,538 shares in order to effect the stockholders' control over the new company "immediately upon the conveyance of all of the assets of the Old Company". (R. 7.) Such stock control was an express condition of the corporate distribution. In giving effect to the agreement, immediately upon the conveyance to respondent of

the old company's assets, legal title to all the 174,538 shares vested (even though momentarily as to the part in question) in the stockholders, to whom passed the old company's inherent right to receive the stock. *Raybestos-Manhattan Co.* v. *United States, supra.* Neither the issuance nor the delivery by respondent to the stockholders of stock certificates was essential to effect delivery of the stock itself. Certificates, even though required, would merely have evidenced the shares of stock which existed independently thereof. *Pacific Nat. Bank* v. *Eaton,* 141 U. S. 227. And the statute applies as well to "shares" as to "certificates."

Immediately after vesting in the stockholders of legal title to, and the right to receive, respondent's stock, legal title to so much of the stock as was to be sold to the Bankers was placed in Nelson, as a trustee, charged by the stockholders with the duty of transferring the stock to the Bankers, receiving the proceeds and making distribution thereof. Nelson was not appointed by the old company but by its stockholders. And the appointment was irrevocable. Thus, it cannot be contended that the designation by the stockholders of Nelson as their attorney in fact or nominee to receive the stock could have been withdrawn and, therefore, that such designation did not constitute a transfer within the meaning of the Act. It follows that the 61,365 shares received by Nelson as attorney for the other stockholders (thus excluding the 13,173

shares acquired by him as a stockholder) were properly subjected to tax upon the transfer from the stockholders to Nelson of their legal title to and/or their rights to receive such shares and certificates therefor.

2. The argument that the stockholders acquired no right to receive, or legal title to, the shares in question is inconsistent with the concession of respondent below that the tax on the transfer by the old company "to its stockholders" of the right to receive all the shares was valid. (Fdgs. 8, 9, R. 9.) Moreover, the argument finds no support in the opinion of the Court of Claims, which states (R. 12):

> The right to receive the stock of the new company was under the foregoing decision [*Raybestos-Manhattan Co.* v. *United States,* 296 U. S. 60] vested in the old company, and upon the transfer of this right *to its stockholders* the old company paid a stamp tax of $4,020.46, which the plaintiff now concedes it may not recover. [Italics supplied.]

3. The instant case falls squarely within the principles announced in *Raybestos-Manhattan Co.* v. *United States, supra.* The generating source of the right to receive respondent's newly issued shares was the conveyance to it of the property of the old company. The new shares could not lawfully be issued to any other than the grantor corporation without its authority, and that authority could not be exercised for the benefit of third per-

sons other than its own assenting stockholders. The agreement of September 27, 1928, embodied the duty on respondent to issue the new shares upon receipt of the property, and at the same time made disposition to the stockholders of the old corporation of the correlative right to receive the stock. Thus, there was effectively transferred to its stockholders the old company's right to receive respondent's stock quite as much as if the several legal relationships of the parties had been established at different times and by separate documents. This conclusion, we submit, is required by the precise holding in the *Raybestos-Manhattan* case.

The stockholders, having obtained the rights to receive all shares by the express action of the old company, also had the power to command the disposition of all or any part of the stock, or of their rights to receive the stock or certificates therefor, which included the right to direct issuance of legal title and certificates for the stock to some other person. The exercise of that right in favor of Nelson called the statute into operation.

The stockholders' rights to receive the stock and legal title thereto were just as effectively transferred to Nelson by the method followed as if certificates for the stock had been first issued to the stockholders and then endorsed and surrendered by them with directions to reissue in the name of Nelson. It cannot be doubted that there would then have been a taxable transfer. What

was said in the *Raybestos-Manhattan* case, *supra,* at 63, is equally applicable here:

> We think that this effective disposition of the right to receive the stock involved a taxable transfer quite as much as if the several legal relationships of the parties had been established at different times and by separate documents. * * * The reach of a taxing act whose purpose is as obvious as the present is not to be restricted by technical refinements.

4. It may be assumed that Nelson had no beneficial interest in the shares transferred by the stockholders. But there is no requirement in the statute that there be a beneficial interest in the transferee, or even that the right to receive the shares shall be unconditional at the time of transfer. *Founders General Corp* v. *Hoey,* 84 F. (2d) 976 (C. C. A. 2d), pending on certiorari, No. 398, present Term. The statute expressly negatives the requirement of beneficial interest, taxing the transfer "whether entitling the holder in any manner to the benefit of such stock, interest, or rights, or not." (Schedule A–3, *infra,* p. 21.) Regulations 71, Article 34 (u) (*infra,* p. 22), similarly provide that "Transfers of stock are subject to the tax even though the holders thereof are not entitled in any manner to the benefit of the stock." If Nelson be regarded as a trustee for the stockholders, the transfer is recognized as taxable by Article 34 (c) of Regulations 71, *infra,* p. 22.)

The court below, in its opinion, cites with apparent approval *National Bond & Share Corp* v. *Hoey,* 14 F. Supp. 787 (S. D. N. Y.). That case was overruled by the United States Circuit Court of Appeals for the Second Circuit in *Founders General Corp.* v. *Hoey, supra.* The conclusion reached by the Court of Claims is in accordance with the decision in *Unión Trust Co.* v. *Heiner,* 26 F. (2d) 391 (W. D. Pa.), and the cases following it. These and the instant case are, we believe, in conflict with *Founders General Corp* v. *Hoey, supra,* and with the reasoning of this Court in the *Raybestos-Manhattan* case. These cases are discussed in our brief filed in *United States* v. *A. B. Leach & Co.,* No. 331, present Term; the discussion will not be repeated here, but reference thereto is respectfully made.

CONCLUSION

For the reasons stated, the judgment of the court below should be reversed and the case remanded with directions to enter judgment for respondent only as to the 13,173 shares belonging to Nelson.

Respectfully submitted.

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DECEMBER 1936.

APPENDIX

Revenue Act of 1926, c. 27, 44 Stat. 9:

SEC. 800. On and after the expiration of thirty days after the enactment of this Act there shall be levied, collected, and paid, for and in respect of the several bonds, debentures, or certificates of stock and of indebtedness, and other documents, instruments, matters, and things mentioned and described in Schedule A of this title, * * * the several taxes specified in such schedule. * * * (U. S. C., Title 26, Sec. 900.)

SCHEDULE A—STAMP TAXES

* * * * *

2. Capital stock, issue: On each original issue, whether on organization or reorganization, of certificates of stock, or of profits, or of interest in property or accumulations, by any corporation, on each $100 of face value or fraction thereof, 5 cents: *Provided,* That where a certificate is issued without face value, the tax shall be 5 cents per share, unless the actual value is in excess of $100 per share, in which case the tax shall be 5 cents on each $100 of actual value or fraction thereof, or unless the actual value is less than $100 per share, in which case the tax shall be 1 cent on each $20 of actual value, or fraction thereof.

The stamps representing the tax imposed by this subdivision shall be attached to the stock books and not to the certificates issued.

3. Capital stock, sales or transfers: On all sales, or agreements to sell, or memoranda

of sales or deliveries of, or transfers of legal title to shares or certificates of stock or of profits or of interest in property or accumulations in any corporation, or to rights to subscribe for or to receive such shares or certificates, whether made upon or shown by the books of the corporation, or by any assignment in blank, or by any delivery, or by any paper or agreement or memorandum or other evidence of transfer or sale, whether entitling the holder in any manner to the benefit of such stock, interest, or rights, or not, on each $100 of face value or fraction thereof, 2 cents, and where such shares are without par or face value, the tax shall be 2 cents on the transfer or sale or agreement to sell on each share: * * * (U. S. C., Title 26, Sec. 902).

Treasury Regulations 71, approved July 7, 1928, promulgated under the Revenue Act of 1926:

ART. 31. *Basis of tax.*—Every transfer or sale of stock, either before or after issuance of a certificate, is taxable. The tax accrues at time of making the sale or agreement to sell or memorandum of sale, or delivery of, or transfer of the legal title to shares, or certificates of stock, or of profits, or of interest in property or accumulations in any corporation, joint-stock company, or association, or of the right to subscribe for or to receive such shares or certificates, regardless of the time or manner of the delivery of the certificate or agreement or memorandum of sale.

ART. 34. *Sales and transfers subject to tax.*—The following transactions are subject to the tax:

(a) The sale, or transfer, or change of ownership, of certificates of stock, or of

profits, or of interest in property or accumulations in corporations, joint-stock companies, or associations.

(b) The sale or transfer of shares of stock, whether or not represented by certificates.

(c) The transfer of stock to or by trustees.

* * * * *

(g) The transfer of the interest of a subscriber for stock, however such interest may be evidenced or conditioned upon further payments.

(h) The transfer of the right to subscribe for stock in any corporation, joint-stock company, or association, whether or not evidenced by warrants.

* * * * *

(t) The transfer of the right to receive stock which a corporation has unconditionally agreed to issue.

(u) Transfers of stock are subject to the tax even though the holders thereof are not entitled in any manner to the benefit of the stock.

U. S. GOVERNMENT PRINTING OFFICE: 1936